

Macro Note

Malaysia: Inflation Steadied At 2.0% In Aug

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- Headline inflation maintained at 2.0% y/y in Aug, matching Bloomberg consensus but coming in a tad lower than our estimate of 2.1%. The steady inflation rate was largely thanks to favourable base effects and a continuation of government subsidies particularly on fuels, chicken, eggs, and cooking oil. This helped to counterbalance the significant rise in prices of some essential food items (i.e. rice, fresh meat, and fish & seafood), water and electricity bills, pharmaceutical products, transport services, and education during the month.
- We stick to our view that inflation will likely hover around 2.0% in the remainder of the year, keeping our 2023 full-year inflation forecast of 2.8% intact (BNM est: 2.8%-3.8%, 2022: 3.3%). For 2024, upside risks to the inflation outlook has heightened as global energy prices rebound to above USD90/bbl levels and the effects of El Nino on staple food especially rice become more imminent, in addition to the Malaysian government's plan to rationalize its subsidies next year. While awaiting the detailed announcement on subsidy rationalization by the government, we keep our 2024 full-year inflation forecast unchanged at 2.8% for now.
- With the costs of living remaining elevated, domestic growth momentum softening and the persistent of slight labour market slack amid tighter global financial conditions, we believe that Bank Negara Malaysia (BNM) will extend its policy rate pause at the final meeting of this year (on 1-2 Nov) and throughout 2024. The fourth month of positive real interest rates will also give the central bank breathing room at this juncture. In anticipation of potential supportive measures and fiscal reform policies unveiled in the coming Budget 2024 (on 13 Oct), higher domestic growth for 2024, and Fed rate cuts come into focus in 2H24, we think that rate cuts by BNM next year are off the table.

Softer Core Inflation In Aug

Headline inflation maintained at 2.0% y/y in Aug, matching Bloomberg consensus but coming in a tad lower than our estimate of 2.1%. Compared to previous month, the consumer price index (CPI) rose 0.2% (Jul: flat), with 74.8% or 413 out of 552 items recording price increases (Jul: 75.4% or 416 items). Of which, 399 items registered a price hike of less than or equal to 10% (Jul: 399) while 14 items recorded a price increase of more than 10% (Jul: 17 items). This compared with 96 items that showed a decline in prices (Jul: 94) and 43 items that saw stable prices (Jul: 42 items). Year-to-date (YTD) as of Aug, headline inflation averaged 2.9% (Jan-Aug 2022: +3.0%).

The steady annual inflation rate in Aug was largely thanks to favourable base effects and a continuation of government subsidies particularly on fuels, chicken, eggs, and cooking oil. This helped to counterbalance the significant rise in prices of some essential food items, utility bills, pharmaceutical products, transport services,

and education in the month. Hence, food price inflation decelerated further to 4.2% y/y (from +4.3% in Jul) while non-food price inflation rebounded to 1.0% (from +0.8% in Jul).

- **Food & non-alcoholic beverages** price inflation moderated to 4.1% y/y last month (from +4.4% in Jul), thanks to a persistent slowdown in price inflation of both food at home (Aug: +2.9%, Jul: +3.0%) and food away from home (Aug: +5.9%, Jul: +6.2%). That said, several essential food items recorded a price hike during the month, namely rice (Aug: +3.0%, Jul: +2.4%), fresh meat (Aug: +6.0%, Jul: +5.3%), and fish & seafood (Aug: +1.5%, Jul: +1.1%).
- **Transport** price component registered a flat y/y growth (Jul: -0.4%), largely thanks to steady fuel pump prices. It helped to offset the gain in prices of transport services (Aug: +3.5%, Jul: +1.4%).
- Conversely, **housing, water, electricity, gas & other fuels** price inflation edged up to 1.8% (from +1.7% in Jul), primarily driven by costlier water (Aug: +2.1%, Jul: flat) and electricity (Aug: +2.0%, Jul: flat) bills.
- **Healthcare** price inflation jumped to 2.4% (Jul: +2.0%), the highest level since Oct 2017. This was primarily due to pricier pharmaceutical products (Aug: +2.8%, Jul: +1.8%).
- **Education** price inflation also accelerated for a second straight month to 2.1% (Jul: +2.0%) as a result of price increases in pre-primary & primary education (Aug: +2.8%, Jul: +2.6%), tertiary education (Aug: +0.3%, Jul: +0.1%), and other education services (Aug: +2.7%, Jul: +2.2%).

Meanwhile, **core inflation**, which excludes volatile fresh food prices and price-administered goods, decelerated for a ninth straight month to 2.5% y/y (from +2.8% in Jul). This marks the lowest level since May 2022, but is still higher than headline inflation for 11 months in a row by 0.4ppt (Jul: 0.8ppt). It also remains above its 2016-2022 long-term average level of 1.7% for a 19th month, taking the YTD core inflation to an average of 3.4% in the first eight months of 2023 (Jan-Aug 2022: +2.5%). **Services inflation** tracked the downtrend in core inflation, easing for the ninth consecutive month to 2.7% (from +2.9% in Jul). Notwithstanding that, services inflation continued to stay above its 2016-2022 long-term average level of 2.0% for 16th months in a row.

Risks To Inflation Remain Tilted To The Upside

Following Jul-Aug headline inflation outturns, we stick to our view that inflation will likely hover around 2.0% in the remainder of the year, keeping our 2023 full-year inflation forecast of 2.8% intact (BNM est: 2.8%-3.8%, 2022: 3.3%). Our view takes into consideration the government's pledge to maintain most of its subsidies for 2H23, an absence of acute global supply shocks, as well as in-house expectations for the currency. While the selling price of imported white rice has been raised by 36.2% to MYR3,200 per tonne, effective from 1 Sep; the price of local white rice remains capped at MYR2.60/kg. Agriculture and Food Security Minister Datuk Seri Mohamad Sabu has also assured that there are enough stockpiles of rice in the country at 900,000mn metric tonnes. It comprises 250,000mn metric tonnes of government stockpiles and 650,000mn metric tonnes of commercial stock that could last for up to five months. He added that the rice supply in the domestic market was also expected to recover in a month. In addition to that, easing core and services inflation further affirms a continuation of disinflation trend in the coming months.

For 2024, upside risks to the inflation outlook has heightened as global energy prices rebound to above USD90/bbl levels and the effects of El Nino on staple food especially rice become more imminent, in addition to the Malaysian government's plan to rationalize its subsidies next year. The government has constantly said that

a targeted subsidy mechanism and progressive wage policy will be implemented next year after the Central Database Hub system is ready by year-end or early 2024. While awaiting the detailed announcement on subsidy rationalization and progressive wage mechanism by the government, we keep our 2024 full-year inflation forecast unchanged at 2.8% for now.

With the costs of living remaining elevated, domestic growth momentum softening and the persistence of slight labour market slack amid tighter global financial conditions, we believe that Bank Negara Malaysia (BNM) will extend its policy rate pause at the final meeting of this year (on 1-2 Nov) and throughout 2024. The fourth month of positive real interest rates will also give the central bank breathing room at this juncture. In anticipation of potential supportive measures and fiscal reform policies unveiled in the coming Budget 2024 (on 13 Oct), higher domestic growth for 2024, and Fed rate cuts come into focus in 2H24, we think that rate cuts by BNM next year are off the table. This is also in view that the current 3.00% overnight policy rate is considered as a neutral rate should real GDP grow between 4.0%-5.0% and underlying demand price pressures are contained in the range of 2.0%-3.0%.

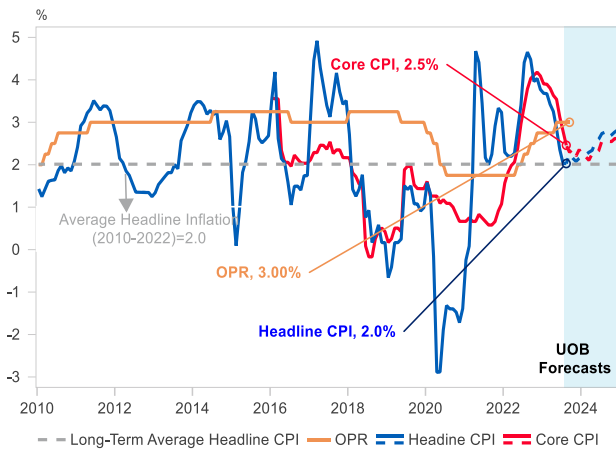
Our Forecast For BNM Rates

Source: Global Economics & Markets Research

%	As of 22 Sep	4Q23	1Q24	2Q24	3Q24
Overnight Policy Rate	3.00	3.00	3.00	3.00	3.00
Statutory Reserve Requirement	2.00	2.00	2.00	2.00	2.00

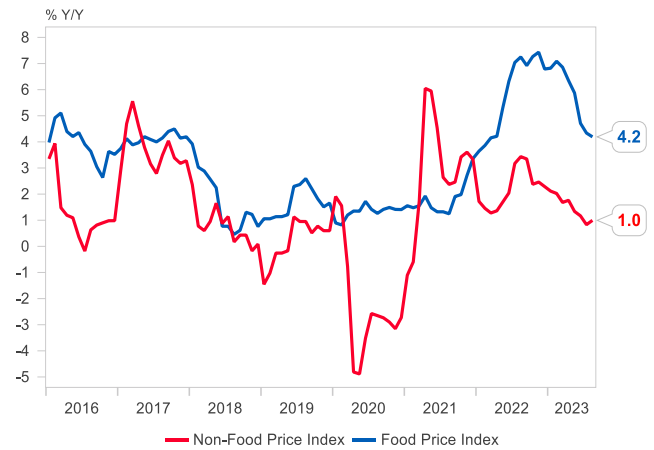
Malaysia's Inflation Vs OPR

Source: Macrobond, UOB Global Economics & Markets Research



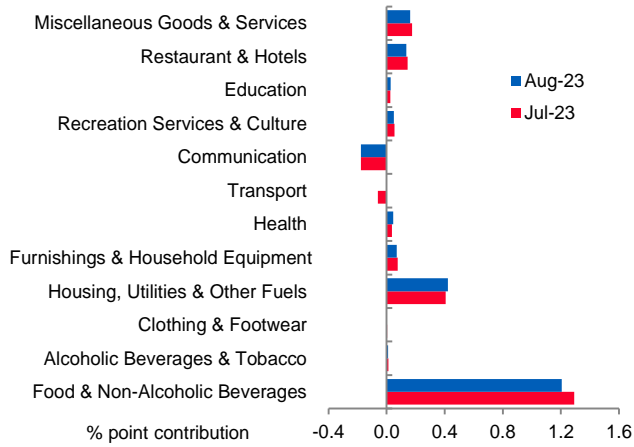
Food Price Inflation Continued To Ease

Source: Macrobond, UOB Global Economics & Markets Research



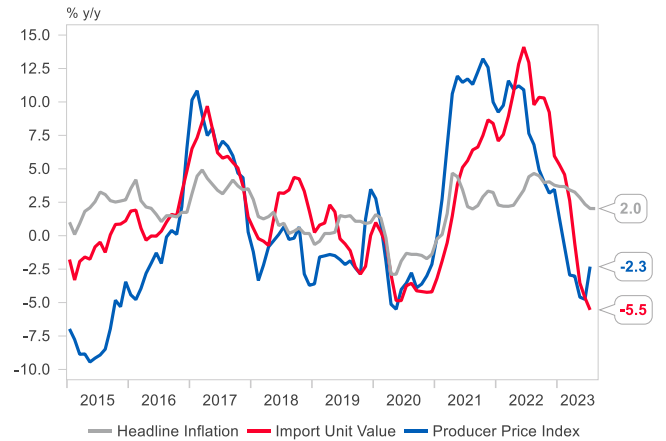
Key Contributors To CPI

Source: CEIC, UOB Global Economics & Markets Research



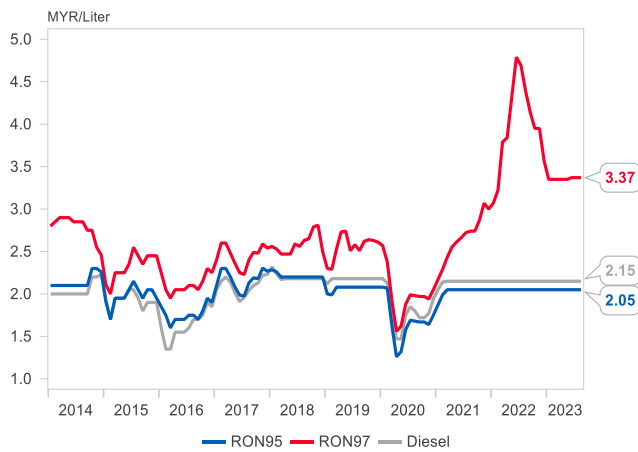
Producer Prices Declined At A Slower Pace Of 2.3% Y/Y In Jul

Source: Macrobond, UOB Global Economics & Markets Research



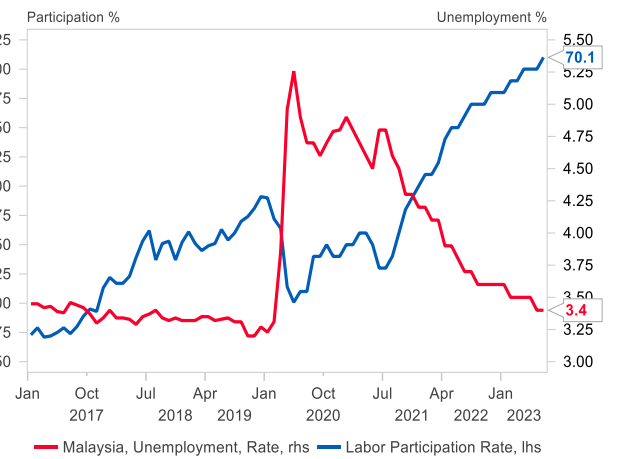
Average Monthly Fuel Pump Prices

Source: MOF, Macrobond, UOB Global Economics & Markets Research



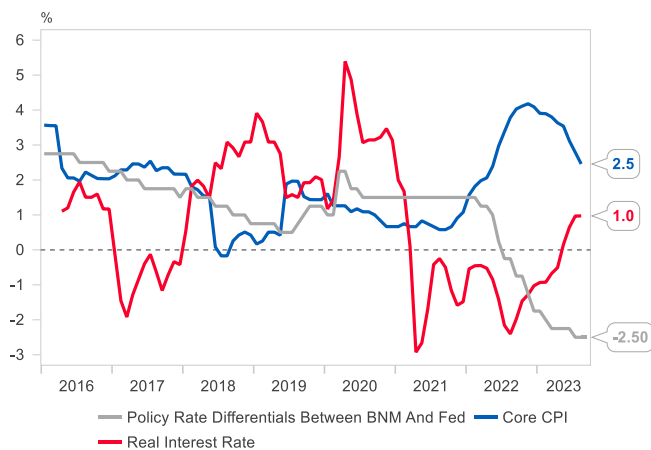
Labour Market Conditions

Source: Macrobond, UOB Global Economics & Markets Research



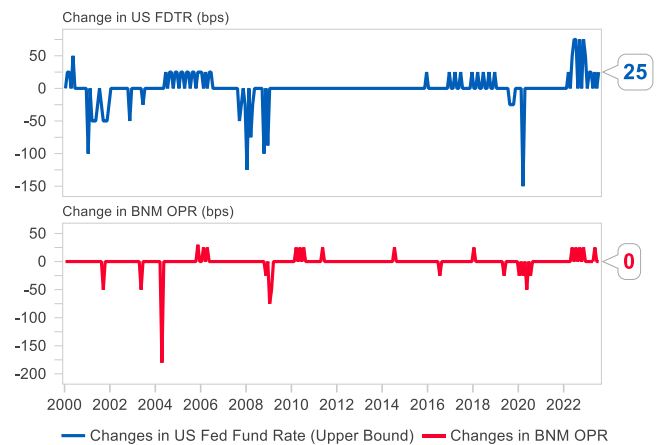
Real Interest Rates (OPR Less CPI) Remained Positive In Aug

Source: Macrobond, UOB Global Economics & Markets Research



Historical Changes In US Fed Rates And OPR

Source: Macrobond, UOB Global Economics & Markets Research



Malaysia's CPI Components: % Y/Y Change

Source: Macrobond, UOB Global Economics & Markets Research

Headline CPI Component	12/2022	1/2023	2/2023	3/2023	4/2023	5/2023	6/2023	7/2023	8/2023
All Items	3.8	3.7	3.7	3.4	3.3	2.8	2.4	2.0	2.0
Food & Non-Alcoholic Beverages	6.8	6.7	7.0	6.9	6.3	5.9	4.7	4.4	4.1
Food at Home	4.9	5.1	5.8	5.6	5.0	4.3	3.2	3.0	2.9
Food Away from Home	9.6	9.3	8.9	8.6	8.1	8.1	6.8	6.2	5.9
Alcoholic Beverages & Tobacco	0.7	0.8	0.8	0.6	0.6	0.7	0.6	0.5	0.5
Clothing & Footwear	0.4	0.5	0.4	0.5	0.5	0.4	0.1	0.1	0.0
Housing, Water, Electricity, Gas & Other Fuels	1.5	1.5	1.7	1.6	1.6	1.8	1.8	1.7	1.8
Actual Rental For Housing	1.6	1.6	1.9	1.9	1.9	2.1	2.1	2.1	1.9
Maintenance & Repair of Dwelling	3.7	3.5	3.3	2.7	2.5	1.6	1.4	1.0	0.9
Water Supply & Miscellaneous Services	0.6	1.1	1.2	1.2	1.2	1.2	0.8	0.8	2.4
Electricity, Gas & Other Fuels	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	1.6
Furnishings, Household Equipment & Maintenance	3.7	3.5	3.4	3.1	3.0	2.7	2.3	1.9	1.7
Health	1.3	1.6	1.8	2.2	2.1	1.9	2.0	2.0	2.4
Transport	4.9	4.0	3.7	2.4	2.3	1.0	0.0	-0.4	0.0
Purchase of Vehicles	2.0	2.1	1.9	2.1	2.1	2.0	1.9	1.3	0.7
Operation of Personal Transport Equipment	4.3	3.3	2.9	1.6	1.5	0.5	-0.6	-0.8	-0.3
Transport Services	17.8	17.9	18.8	13.9	13.5	6.7	5.2	1.4	3.5
Communication	-0.1	-1.4	-1.4	-1.4	-1.4	-3.7	-3.6	-3.7	-3.7
Recreation Services & Culture	2.4	2.7	1.7	1.9	1.8	1.8	1.6	1.1	1.0
Education	1.4	1.3	1.6	1.7	1.6	1.9	1.9	2.0	2.1
Restaurant & Hotels	7.4	6.8	7.4	7.2	6.6	6.7	5.4	5.0	4.7
Miscellaneous Goods & Services	2.3	2.3	2.5	2.1	2.5	2.9	2.6	2.6	2.4

Malaysia's Inflation Tracker

Source: Macrobond, UOB Global Economics & Markets Research

Indicator	12/2022	1/2023	2/2023	3/2023	4/2023	5/2023	6/2023	7/2023	8/2023
Economic Measures									
Headline CPI	3.8	3.7	3.7	3.4	3.3	2.8	2.4	2.0	2.0
Core CPI	4.1	3.9	3.9	3.8	3.6	3.5	3.1	2.8	2.5
PPI	3.5	1.3	-0.8	-2.9	-3.0	-4.6	-4.8	-2.3	N/A
Commodities Prices									
Brent Crude, Spot	8.7	-4.3	-15.3	-24.4	-24.6	-38.0	-31.2	-20.8	-8.6
CPO, Spot	-21.4	-33.3	-38.8	-35.4	-44.8	-47.7	-26.4	-9.4	-5.7
GSCI Commodities	26.0	12.8	-0.3	-10.0	-15.1	-24.1	-14.2	-5.0	-1.8
GSCI Industrial Metals	-7.6	-1.9	-15.7	-21.0	-17.0	-17.5	-3.8	1.8	0.3
GSCI Softs	-2.0	1.0	3.3	-1.0	9.1	7.5	11.6	22.9	15.6
Baltic Dry Index	-31.7	-52.0	-51.5	-41.1	-34.4	-61.9	-51.3	-40.5	12.5

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